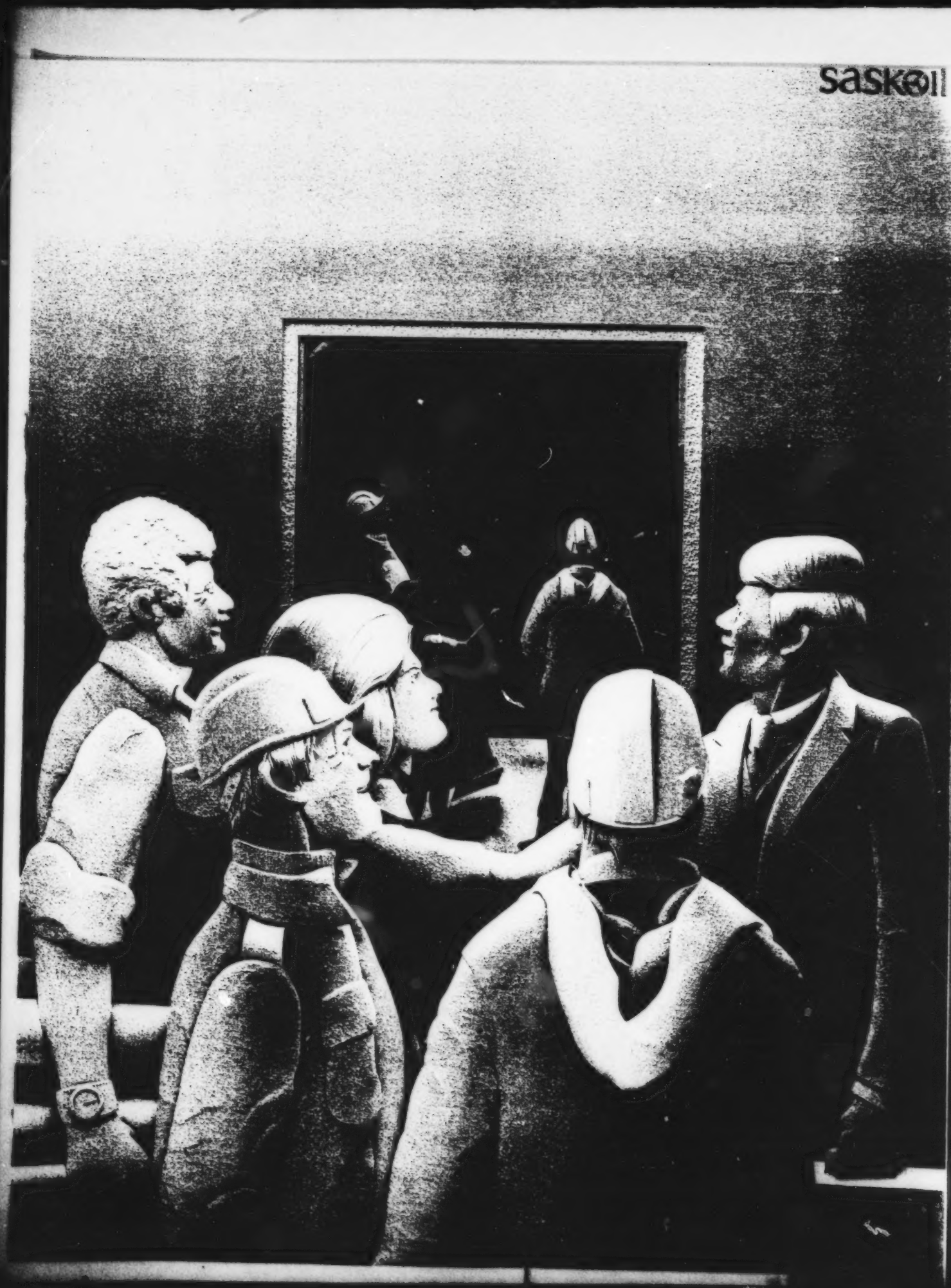
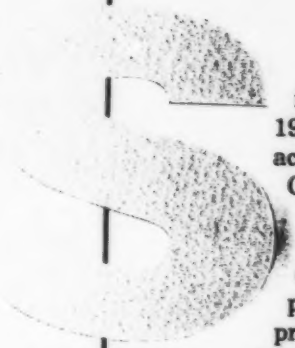

saskoil

PROFILE



Since our inception in 1973, we have been an active member of the Canadian petroleum industry. Solely an upstream resources company, we explore for, develop, produce, and market crude oil and natural gas. In terms of oil production, we rank among the top three oil companies in Saskatchewan and among the top 20 in Canada.

Although operations are conducted in all three prairie provinces, approximately 98 percent of our total revenue is generated from oil properties located in Saskatchewan. Of our total production, 90 percent is exported to the United States. Light and medium oils account for 60 percent of total production, with the remainder being heavy oil. Natural gas production is minimal compared to crude oil production. We operate 45 percent of our production and have a broad network of joint venture partners.

Saskoil has a mineral interest in 302 thousand net hectares of land. Three quarters of our land base is located in Saskatchewan.

Saskoil is a publicly held company with shares traded on the major Canadian stock exchanges. The Province of Saskatchewan is the majority equity owner, with the remaining shares widely distributed across the country.

The company is in a strong financial position with low debt and significant liquid assets. Long term debt as a percentage of debt and shareholders' equity was 5.3 percent after completion of the public share issue.

Saskoil had 284 permanent employees at year end. Of this number, 217 work at our head office in Regina and 67 at our field offices in Estevan, Swift Current, Coleville, and Maidstone.

In-house training programs, job related education and career planning continue to be emphasized in order to improve existing skills and ensure individual employees achieve their potential.

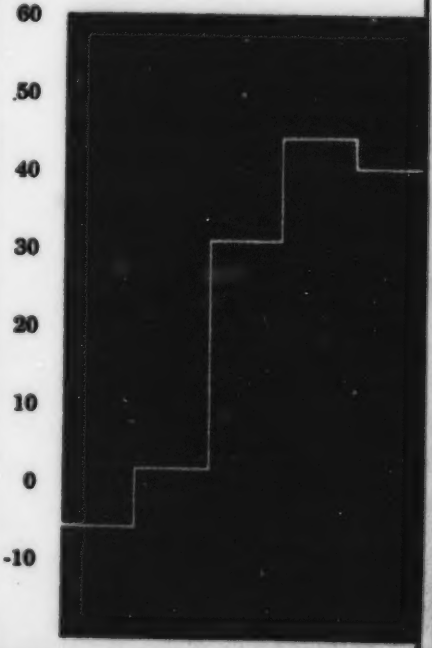
During 1985, Saskoil received approval from the Saskatchewan Human Rights Commission for an affirmative action program. Affirmative action is a recruitment strategy designed to focus on three target groups: people of Indian ancestry, the disabled, and women.

ABOUT OUR COVER

Saskoil is proud to include in our annual report the cover illustration entitled "Transition" by world famous papersculpture artist, Johnathan Milne. Johnathan has captured in an imaginative way the transition of Saskoil from a Saskatchewan crown corporation to a publicly held company. He is an internationally recognized artist who works in a unique style of illustrating in paper. He is reputed to be the best in the world using this medium and has many fine pieces in collections of corporations and galleries throughout Canada, the United States, Britain, and Australia. The original is located at Saskoil's main reception area in Saskoil Tower in Regina, Saskatchewan.

EARNINGS

(millions of dollars)



ACHIEVEMENTS

- During 1985, Saskoil issued $110 million of common and convertible preferred shares, transforming the company from a wholly owned Saskatchewan crown corporation to a publicly held company that is responsible to a broader shareholder base.
- In December, Saskoil concluded the development of its Marsden Waterflood Project — the largest operated capital project in Saskoil's history. Completed at a cost of $14 million, the Marsden waterflood is expected to more than double the recoverable reserves in the field.
- By becoming less dependent on a single purchaser and by obtaining favourable contract terms from purchasers, Saskoil achieved greater stability in the marketing of its oil production.
- Saskoil retired $25 million of debt that matured during 1985. The only long term debt that remains outstanding is a $15 million Participation Bond issue that is due in 1990.

Saskoil Tower: Saskoil's Head Office at 1945 Hamilton Street, Regina, Saskatchewan. ▼

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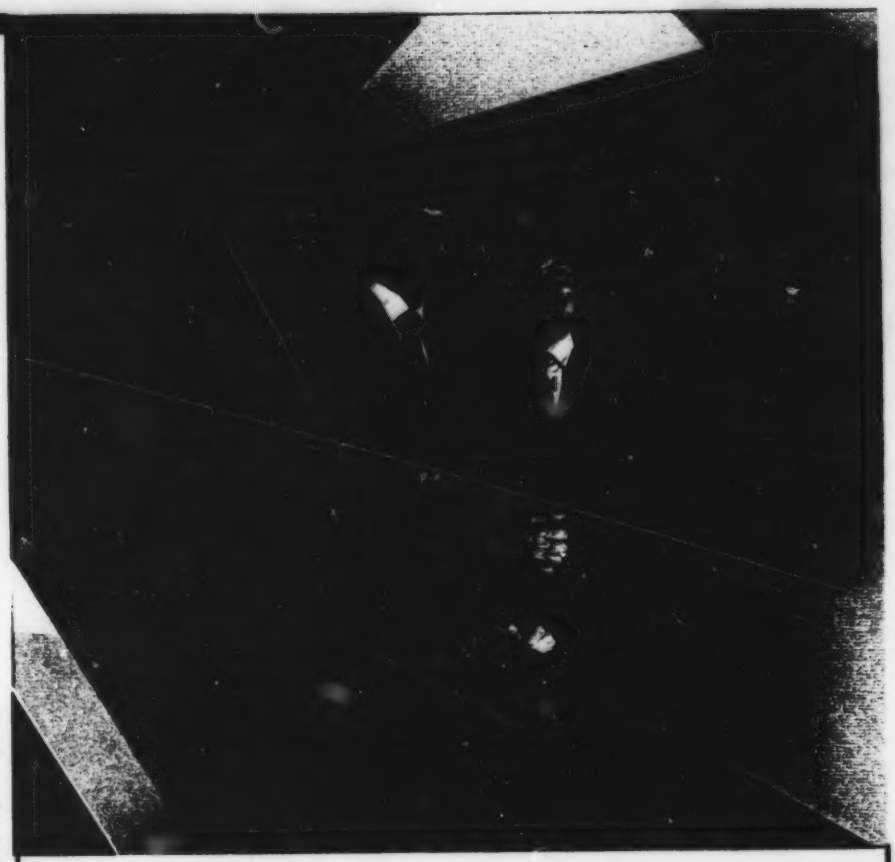
FINANCIAL HIGHLIGHTS

	1985	1984
	(thousands of dollars)	
Crude oil and natural gas sales	161,120	160,935
Earnings	40,623	44,033
Funds provided from operations	63,994	63,578
Dividends	75,000	6,605
Working capital, end of year	22,408	14,834
Total assets	284,529	273,889
Long term debt	15,000	15,000
Return on average capital employed — annual	18.3%	21.8%
Return on average capital employed — four year	16.3%	12.2%

MESSAGE TO THE SHAREHOLDERS



Herb Pinder Jr., Chairman; William Douglas, President and Chief Executive officer.

The past year was successful and exciting for us. It was highlighted by the most significant event in our 12 year history: the initial public offering of Saskoil shares. The $110 million issue of units consisting of one common and two preferred shares was fully subscribed within days of the offering. We are now responsible to shareholders from virtually every part of Canada. The strength of this response reflected investor confidence in the western Canadian oil industry and, particularly, in Saskoil.

We are also pleased to report favourable financial results during 1985. Crude oil and natural gas sales reached a new high of $161.1 million. Funds from operations were $64 million, and earnings were $40.6 million — second only to the record level of earnings established in 1984.

These results enhanced an already strong financial position. During the year, $25 million in debt was retired, leaving only $15 million long term debt outstanding. Cash on hand was $24.2 million at year end.

Beyond our financial accomplishments, we enjoyed an eventful and productive year in all areas of operations. We implemented a $14 million ($10 million net) waterflood recovery scheme at Marsden — our largest operated project ever. We participated in the drilling of 652 exploratory and development wells — a new record for our company. These initiatives have provided the groundwork for future production and revenues.

REVIEW OF OPERATIONS

Our 1985 operations were designed to support the attainment of two fundamental and long term strategic objectives without unduly impairing short term profitability. The first key objective is revenue stability through the diversification of our markets and product streams while the second is revenue growth by tapping our major source of future reserve additions: the increased recovery of oil from existing reservoirs.

In 1985, Saskoil's strong cashflow permitted an aggressive capital program of $58.8 million, a 33 percent increase from 1984. Of this expenditure, 38 percent was directed to exploration for oil and gas and 62 percent was spent on developing previous discoveries and on production facilities improvement.

More specifically, exploration expenditures for land were $7.6 million, resulting in the acquisition of 55 thousand net hectares. During the year, we participated in the drilling

of 86 exploratory wells which yielded 39 oil wells and 10 gas wells. The focus of our exploration activity was threefold: a base program centred in the light oil regions of southern Saskatchewan and Manitoba and the heavy oil areas in central Saskatchewan and Alberta; a higher risk/reward program in northern Alberta; and a natural gas exploration program in Saskatchewan. The latter two initiatives are key components of our diversification plans.

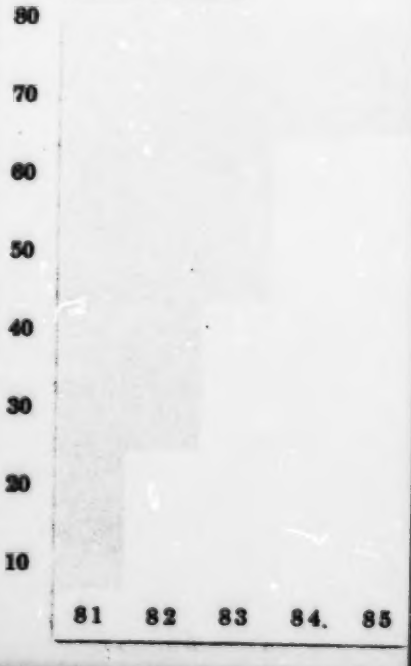
Our primary development drilling was directed towards the mature light and medium oil regions of southeastern Saskatchewan and on Viking light oil pools in the southwest.

Improved recovery projects accounted for 17 percent of the total capital spending in 1985. The waterflood project at Marsden is expected to more than double recoverable reserves and increase the productive capacity of the field. However, the full benefits will not be evident until 1987 when peak production will be reached. The Marsden field has been a prolific producer for years and contributed $5 million to revenues in 1985. A design for an enhanced oil recovery pilot project at Senlac was completed in 1985. This project will proceed in 1986, pending regulatory and partner approval. Our ability to increase reserves at a reasonable cost through these types of projects is critical to our future success.

Oil reserve additions resulting from the success of our drilling program amounted to 621 thousand cubic metres — equivalent to 80 percent of the year's production. As in previous years, we have taken a conservative approach in recording our annual reserve additions. We expect additional reserves as a result of our 1985 infill drilling. However, we will not book these reserves until well production history verifies that incremental volumes are being recovered from the pools. At year end, proven producing oil reserves totalled 6.87 million cubic metres.

FUNDS FROM OPERATIONS

(millions of dollars)



Due mainly to transportation constraints, our production volume of 779 thousand cubic metres of oil in 1985 was only slightly below our record level of 1984. Demand for our crudes continued to be strong. We took advantage of the opportunity provided by market deregulation to diversify and realign our crude oil sales contracts.

MESSAGE TO THE SHAREHOLDERS

OUTLOOK

With the transition to freer markets comes direct exposure to the uncertainties of the world oil market. This report would not be complete without commenting on recent events in the external environment and explaining how Saskoil will respond. It also serves to point out the importance of Saskoil's long term strategic objectives of revenue diversification and improved recovery.

Since November 1985, world oil prices have dropped by more than a third to below $20 (U.S.) a barrel. The middle east OPEC countries have indicated they will continue "over producing" until non-OPEC production levels drop and OPEC regain what they believe to be an appropriate market share based on their reserve levels and production capacity.

While Saskoil has made progress towards lessening our vulnerability to such events, at the current time virtually all revenue comes from crude oil production, the price of which is determined by world markets. Therefore, the impact of prolonged price decreases on revenues, cashflow, and earnings is severe.

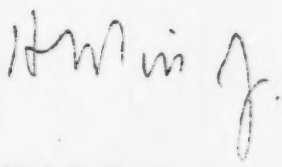
We envision two distinct price scenarios, both supply oriented. First, the oversupply of oil on the market will force both OPEC and non-OPEC nations to adhere to some form of production discipline. Alternately, if a mechanism for production control is not forthcoming, the price itself will inhibit future investment and perhaps shut in some existing production that is more expensive to operate. Either scenario will result in a supply/demand balance leading to price increases, likely in less than a year, but not back to the levels seen in the early 1980's.

Another source of concern is the Saskatchewan royalty structure. The royalty holiday program which has been vital to the success of industry in Saskatchewan is due to expire at the end of 1986. A large proportion of our revenue comes from oil production located in Saskatchewan which is subject to the highest royalty rates in Canada.

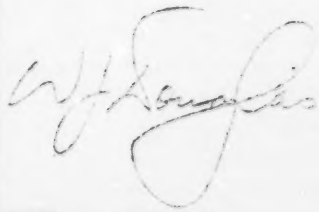
In the longer term, we must be patient and confident in our company's strengths and continue to work towards our strategic objectives. Due to our strong financial position and our substantial reserves and production base, Saskoil is in an enviable position to weather difficult times.

As long as the industry is characterized by uncertainty and volatility, our challenges are clear. We will closely monitor the effectiveness of our capital program to ensure that our expenditures increase our net worth and provide a reasonable return on investment. Our conventional capital program will continue to be funded through internal cashflow and will balance short term needs with those of the longer term. We will continue to maintain a lean overhead and improve the efficiency of existing operations. We will employ innovative marketing strategies to sell our products and will retain our ability to adjust to difficult times and respond to opportunities.

Our sincere thanks go to our employees for their commitment and dedication and for their important contribution to our 1985 achievements. We also express our thanks to the Directors who retired from the Board in 1985 and to our former Vice-Chairman, Paul Schoenhals, who played a vital role in initiating our share offering. We welcome our new Directors as we look to the future with confidence in our growth potential and our ability to reward our shareholders for their investment.

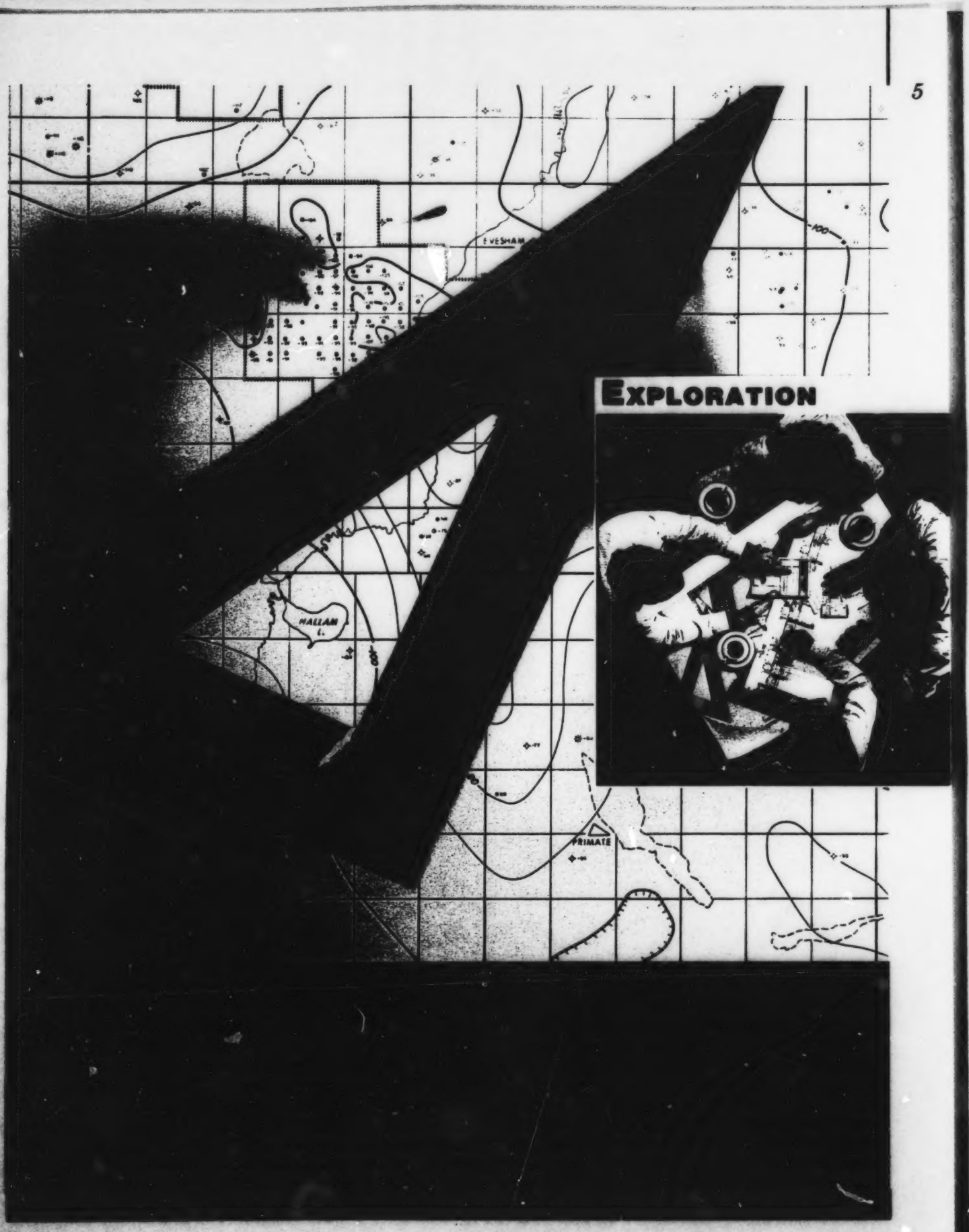


Herb C. Pinder, Jr.
Chairman



William J. Douglas
President
and Chief Executive Officer

Regina, Canada
March 31, 1986


EVESHAM
HALLAM
PRIMATE
EXPLORATION

EXPLORATION

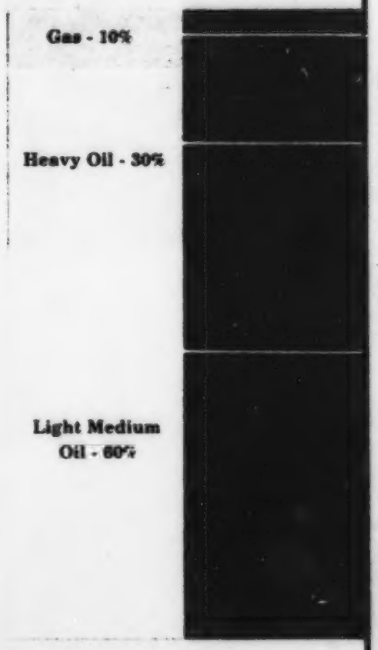
"During 1985 we enjoyed success in our exploration programs. In spite of lower world prices and subsequent lower spending levels, we will continue to pursue our diversification plans in 1986."

Donald Tough
Vice-President, Exploration

Exploration activity in western Canada continued to increase during 1985 as our industry responded to the promise of the Western Accord. In Saskatchewan, the federal deregulation of crude oil together with the extension of the provincial royalty holiday, pushed exploration activities to an all time high. More than 850 exploratory wells were drilled and Crown land sales reached $149 million. Saskoil played an important role in the increasingly competitive Saskatchewan marketplace. Our company participated in the drilling of 86 exploration wells, 53 of which were in Saskatchewan. Of the total wells drilled in 1985, 39 were cased for oil and 10 for gas. We purchased 113 thousand gross hectares (55 thousand net hectares) of mineral rights and shot or purchased 3,200 kilometres of seismic. Exploration expenditures on drilling, seismic, and land acquisitions totalled $22.1 million — a 30 percent increase from 1984.

1985 EXPLORATION EXPENDITURES

By Objective By Activity



LAND

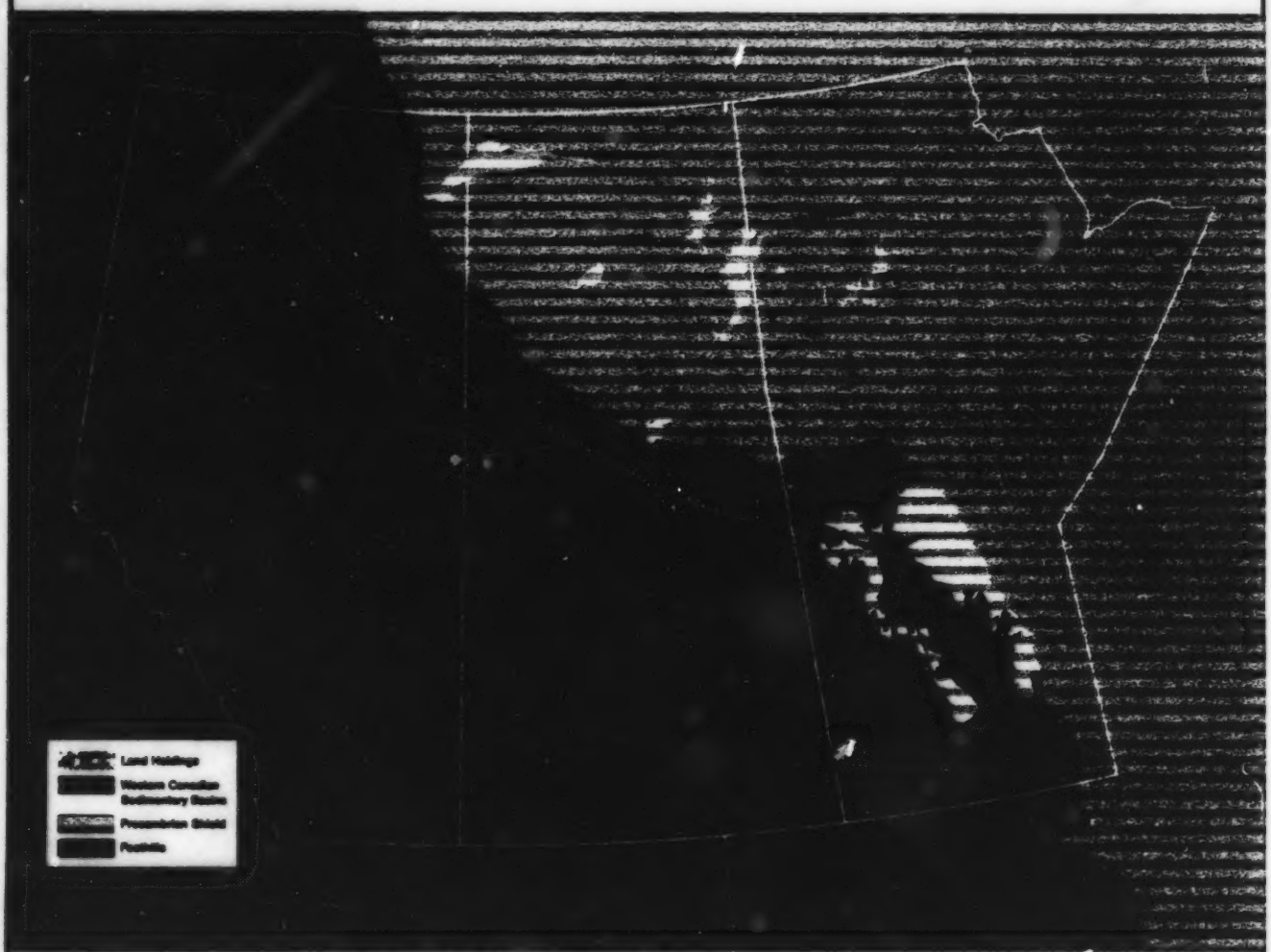
During 1985, we continued to solidify land holdings in all of our key areas of activity across the three prairie provinces. Surpassing our 1984 acquisitions by 96 percent, we purchased 57 thousand gross hectares in Saskatchewan and 56 thousand gross hectares in Alberta/Manitoba. Exploration land purchases amounted to $7.6 million, with development land totalling $0.9 million. Saskoil acquired four percent of all lands tendered in Saskatchewan, becoming the second largest purchaser in the province.

In addition to land purchases, we concluded an agreement with Saskatchewan Power Corporation (SPC) whereby 58 thousand net hectares of Saskoil's mineral rights were assigned to SPC. In return, SPC released to Saskoil 4.5 thousand net hectares of mineral rights and removed its overriding royalty on 55 thousand net hectares of lands which we earned through our 1979 farmin agreement.

Our plans for 1986 will include expansion and development of our current land base, farmin on our active prospects and selective land purchases in order to gain access into promising new areas.

SASKOIL LAND HOLDINGS

(December 31st, 1985)



SASKOIL LAND POSITION

(thousands of net hectares)

	1985	1984	1983	1982
Aquisitions				
Saskatchewan	42	22	6	4
Alberta	10	4	0	1
Manitoba	3	2	6	4
	55	28	12	9
Balance at Year End				
Saskatchewan	233	345	589	752
Alberta	47	75	125	127
Manitoba	22	22	19	19
	302	442	733	898

EXPLORATION

OIL EXPLORATION

Saskatchewan and Manitoba

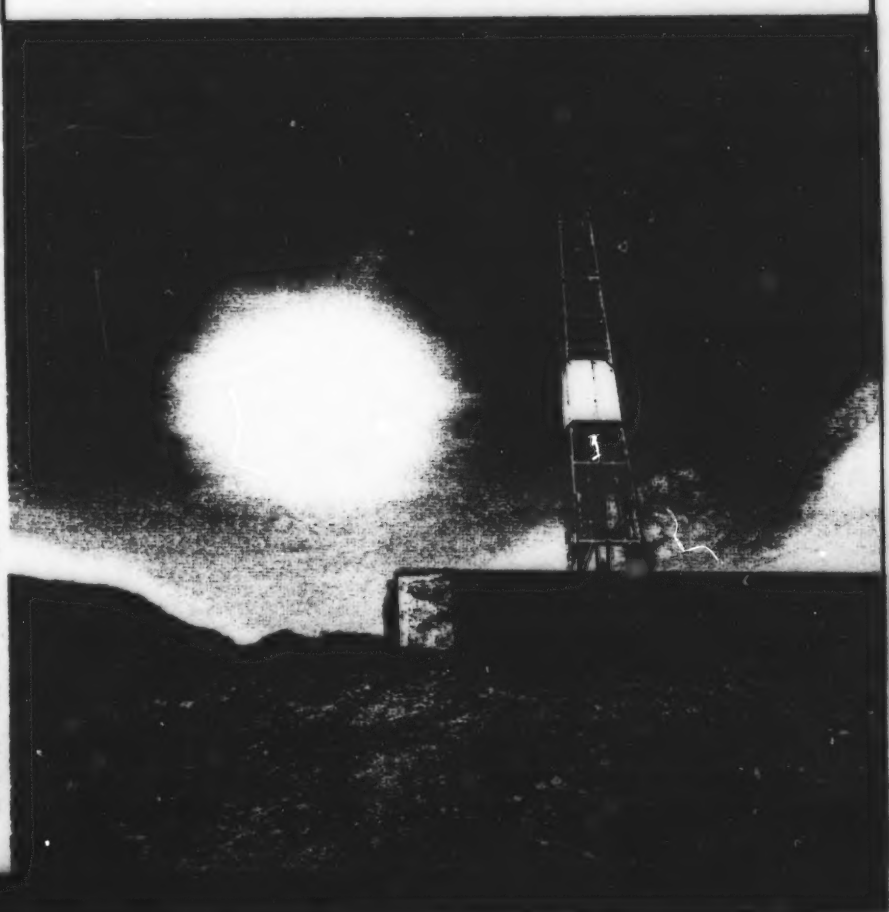
Saskoil has an 18.5 thousand net hectare interest in the Lodgepole light oil play which straddles the Saskatchewan-Manitoba border. By drilling five farmout wells and casing four as potential oil wells, two of our partners earned 50 percent of our interest on the Saskatchewan side of the play at Maryfield. Based on these results, we purchased two drilling reservations and 777 net hectares on this prospect. We now hold an interest in nine thousand gross hectares adjacent to the discoveries and plan to evaluate this prospect more thoroughly in 1986.

Our exploration of the Lodgepole play in Manitoba continued with success on the Routledge and Souris-Hartney prospects. The Routledge well was completed and is producing eight cubic metres per day while development of the remaining spacing units in the pool is scheduled for 1986. Production tests at Souris-Hartney have not been conclusive and further evaluation work is planned for 1986.

In the light oil region south of Weyburn, Saskatchewan, we followed our 1984 evaluation of 135 kilometres of seismic with the drilling of three exploration wells on two prospects. One of the three wells was successful and is currently producing at a rate of four cubic metres per day. Although two of the wells were unsuccessful, we believe further exploration is warranted.

The Swift Current-Rapdan area of southwest Saskatchewan has been a key area of interest in our exploration planning for several years. During 1985, we acquired over 20 thousand net hectares of exploration lands with our working interests ranging from 50 to 100 percent. We based our purchase decision on the interpretation of more than one thousand kilometres of seismic together with the results of drilling evaluation tests. On four prospects in the area, our company participated in the drilling of five wells, four of which were cased for oil. Based on our results to date, we anticipate further drilling in 1986.

During 1985, Saskoil participated in the drilling of 86 exploratory wells, 53 of which were in Saskatchewan. ▼



In central Saskatchewan, bordering Alberta, we continued to focus our heavy oil program on reserves that are recoverable by primary production and which have potential for enhanced oil recovery. In the proximity of our 150 thousand cubic metre Bakken discovery made several years ago at Court, we participated in the drilling of five exploratory wells which resulted in one successful heavy oil well. Although we anticipated more positive results, we are confident that major reserves remain to be discovered and, in 1986, we will continue to pursue this play.

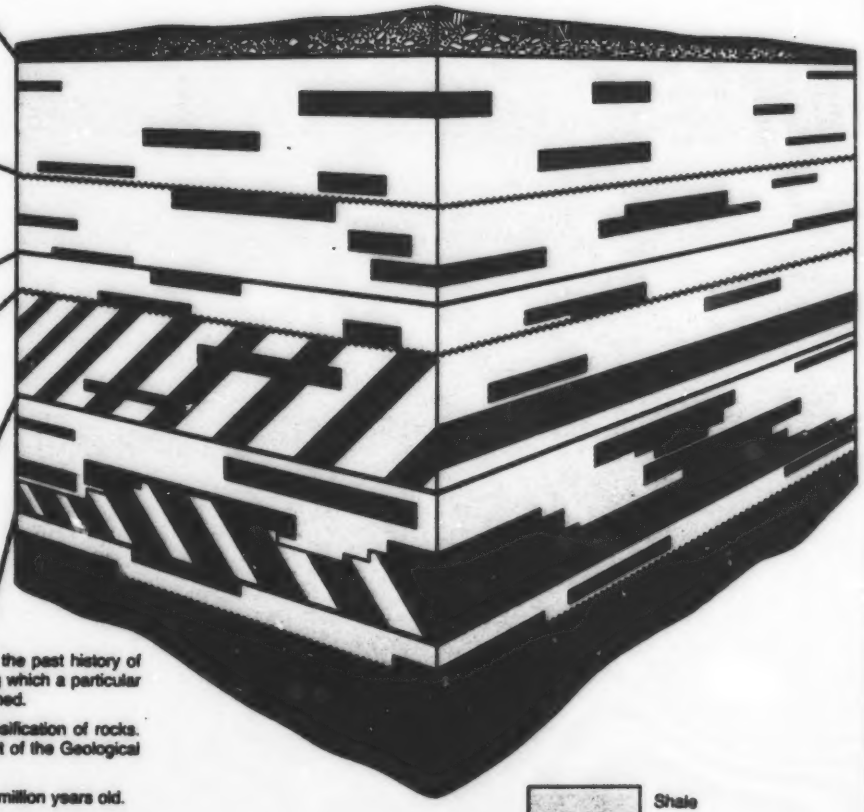
Our heavy oil exploration program on the Mannville play in west central Saskatchewan was highlighted by the drilling of nine wells which resulted in seven cased for production evaluation. Of these successful wells, two were on the Neilburg prospect where we acquired 300 net hectares at Crown land sales. During 1986 our plans include further geological evaluation on this prospect.

Alberta

Our 1984 success on the Keg River play at the Amigo prospect in northwest Alberta continued into 1985. Our success was evident by the drilling of three successful wells which have added 18 cubic metres per day to our production. At the Rainbow Lake prospect on the same play, we participated in the drilling of one successful well with an initial production rate of 175 cubic metres per day. Because of these encouraging results, we have increased our working interests with our partner to 25 and 50 percent in the exploration of these prospects.

GEOLOGICAL MODEL

Geological Age	Area of Saskoil Activity	Formation/ Play
Cretaceous	Western Saskatchewan	Viking Mannville
	Central Alberta	Cardium
	Southwest Saskatchewan	Cantuar
Jurassic	Western Saskatchewan	Roseray
	Southwest Saskatchewan	Shaunavon
Triassic	Northwest Alberta	Halfway
Mississippian	Southeast Saskatchewan/ Manitoba	Charles Mission Canyon Lodgepole
	Western Saskatchewan/ Eastern Alberta	Bakken
Devonian	Southeast Saskatchewan	Birdbear
	Central Alberta	Nisku Leduc
	Northwest Alberta	Keg River



Geological Age: A term used to describe the past history of the earth; the time during which a particular system of rocks was formed.

Formation: A term used for the classification of rocks. The formation is a subset of the Geological age.

Cretaceous Period: Rocks which are 65-135 million years old.

Jurassic Period: Rocks which are 135-190 million years old.

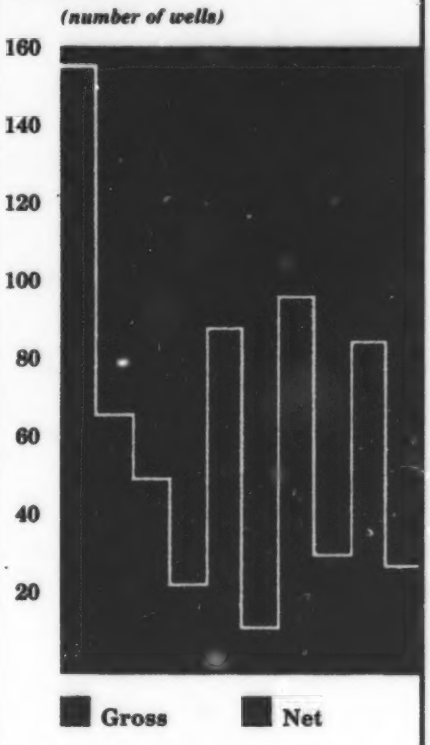
Triassic Period: Rocks which are 195-225 million years old.

Mississippian Period: Rocks which are 320-360 million years old.

Devonian Period: Rocks which are 360-395 million years old.

EXPLORATION

EXPLORATION WELLS DRILLED



In the Frog Lake area, located 90 kilometres northwest of Lloydminster, we participated in our first Alberta Mannville heavy oil play. The Mannville geological formation offers an attractive mix of natural gas and heavy oil recoverable through primary and enhanced oil recovery methods. Through a farmin arrangement, we operated the drilling of five successful heavy oil and/or gas wells. We intend to drill three wells in 1986 to further delineate the oil and gas reserves.

At Wainwright, in east central Alberta, we were successful in one exploratory heavy oil test well. The success from this test well provided us with sufficient encouragement to acquire an additional 120 net hectares at Crown land sales. In early 1986, we plan to drill another well to further evaluate the play.

GAS EXPLORATION

Saskatchewan

In 1985, our gas exploration activity was focused on 3,500 net hectares of potential gas lands that we acquired during the year. Two of the more promising areas we have explored are Beacon Hill-Makwa in northwest Saskatchewan and Leader in the southwest.

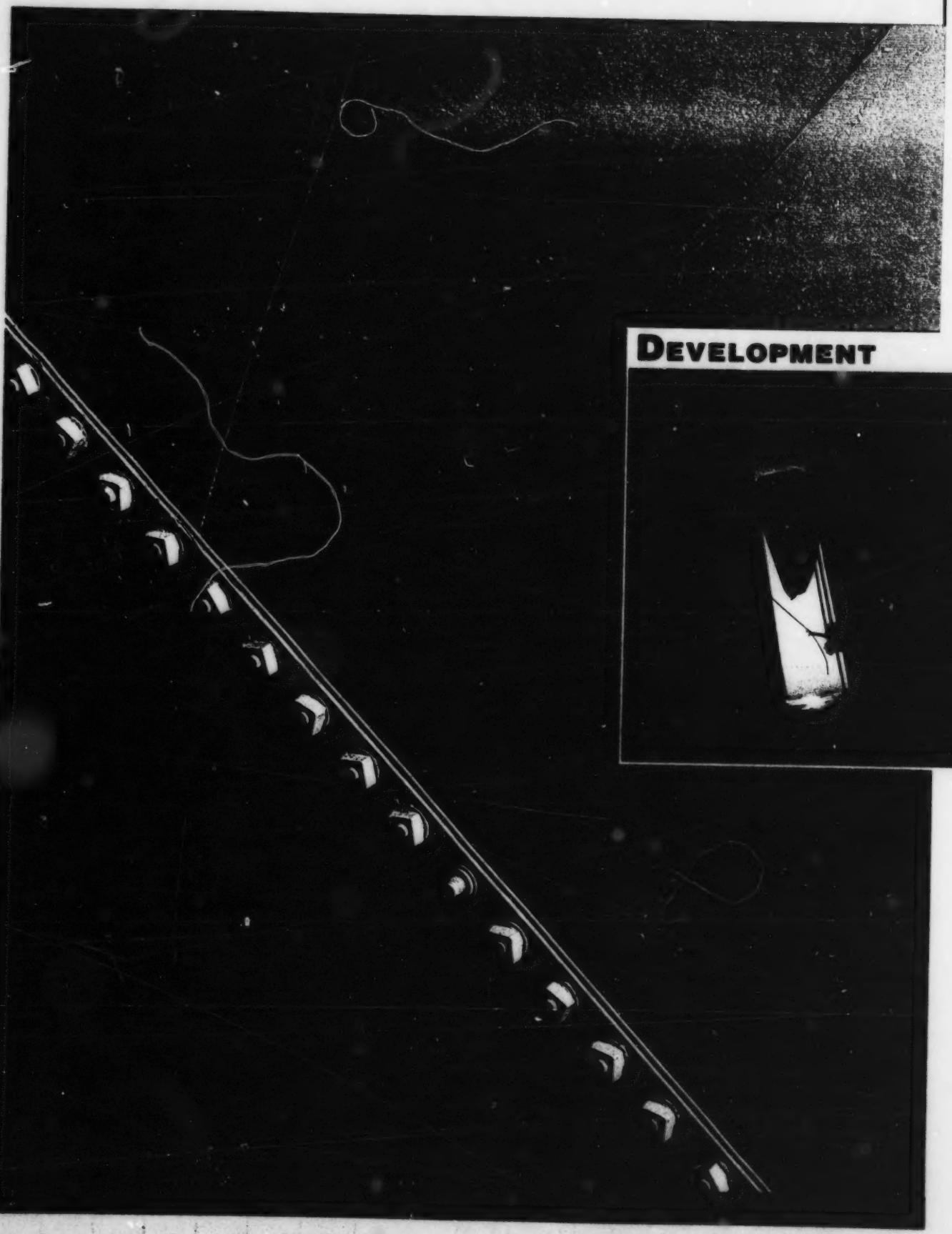
At Beacon Hill-Makwa, we now hold 15 thousand net hectares of land with working interests ranging from 25 to 100 percent. In addition, we have overriding royalty interests on another 38 thousand hectares which were farmed out to a partner in 1982 to 1984. Since our farmout arrangement, our partner has drilled a total of 23 wells resulting in 19 cased gas wells. Further exploration drilling is contingent on a seismic program which was completed in 1985.

In the Leader area, we participated in a 400 kilometre seismic program and acquired two permits at the December Crown land sale. We plan to drill and evaluate this area in 1986 and, given favourable results, attempt to purchase additional lands.

In support of the natural gas industry in Saskatchewan, the Provincial government has committed itself to the attainment of four principal objectives:

1. To double Saskatchewan annual production of natural gas by 1988.
2. To make Saskatchewan self-sufficient in terms of natural gas by 1990.
3. To double Saskatchewan natural gas reserves by 1990.
4. To encourage the exploration for deeper reserves.

In order to take advantage of this improved environment, we have allotted 10 percent of the 1986 exploration capital budget on the development and evaluation of our lands in the gas prone areas of western Saskatchewan. In view of our land position and results to date, we believe that we will be in a favourable position to take advantage of any early marketing opportunities.



DEVELOPMENT

DEVELOPMENT

"The current slump in oil prices simply underscores the need to continue improving oil recoveries in our existing fields."

Dale Christensen,
Vice-President,
Resource Development.

During 1985, our diversified and ambitious development program included the drilling of a record 437 (111 net) working interest development wells, resulting in 415 wells that were cased for production. This program also included construction of gas sales systems, completion or expansion of several major oil treating facilities, and implementation of a waterflood recovery system at Marsden — one of our most prolific heavy oil fields.

In total, 1985 development expenditures were $37.5 million, with $36.6 million spent on capitalized development and $900 thousand on pilot projects.

PRIMARY DEVELOPMENT

Approximately half of Saskoil's development capital was directed toward the drilling and completion of wells capable of producing under their own natural, or "primary", energy. The majority of our primary development activity was centred on the Viking light oil play and on infill drilling projects in Saskatchewan. Proven producing reserve additions of 312 thousand cubic metres were added as a result of primary development.

Light and Medium Oil

Viking Light Oil – Viking pools are characterized by above average initial production rates and low reserves, which combine to create rapid drops in production. In spite of this, Viking wells are an attractive investment under the current royalty structure in Saskatchewan, typically paying back the initial investment within one year. As a participant in the Viking play, we were active in four fields and shared in the drilling of 92 (36 net) wells at a cost of $4.1 million.

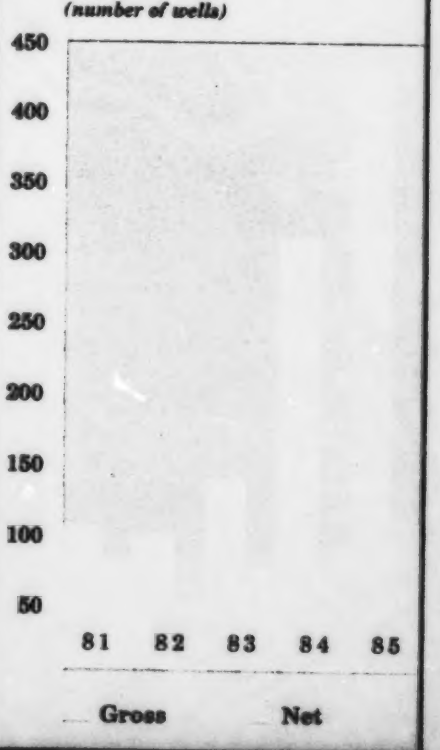
Infill Drilling This process involves drilling between existing wells in order to increase reserves and achieve a more efficient drainage of pools. In 1985, Saskoil spent $3.9 million on several infill drilling projects that yielded 56 (13 net) wells. Our southeast Saskatchewan infill activity included the completion of 1984 programs at Parkman and Queensdale, and smaller programs at Wapella, Whitebear, and Arcola.

Our other light and medium oil development accounted for a total of 20 wells (13 net) drilled at a cost of $4.2 million. In southeast Saskatchewan, six wells were drilled at Weyburn, four at Moose Mountain, and one each at Steelman, Fleming, Queensdale, and Huntoon. In the southwest, drilling occurred at Beverley and Leon Lake, while out-of-province activity included the drilling of two wells at Virden, Manitoba and Bigoray, Alberta.

Heavy Oil

A total of $4.2 million was spent to develop 22 (16 net) heavy oil wells in west central Saskatchewan. This included: four wells each at Evesham, Neilburg, and Marsden; two wells each at Ear Lake, Luseland, and North Smiley; and one well each at Lloydminster, West Buffalo Coulee, Cactus Lake, and Unwin.

DEVELOPMENT WELLS DRILLED



NON-PRIMARY DEVELOPMENT

With the expenditure of $11 million, we expanded our level of activity in non-primary recovery, including waterflood and enhanced oil recovery (EOR) projects. By implementing these types of projects, the amount of oil that can be recovered from a reservoir is greatly increased. The effectiveness of non-primary development can be seen through the addition of 254 thousand cubic metres of oil in 1985 to our proven producing reserves.

Waterflood

This time-proven recovery method is performed by injecting high pressure water into a reservoir, thereby flushing the oil to producing wells.

Marsden The successful implementation of a waterflood in the Marsden heavy oil field was the highlight of our 1985 development program. Jointly owned by Saskoil (76 percent) and Petro-Canada (24 percent), this $14 million waterflood project is the largest operated venture in our history.

At Marsden 27 new wells were drilled, thereby providing the field with the necessary ratio of oil to water wells. The final conversion to a waterflood was realized with the construction of a fuel gas system, the installation of flowlines, and the construction of a water injection plant.

Since the discovery of the Marsden field in 1979, four percent of the original oil-in-place has been produced under primary recovery. By converting to a waterflood program, an additional 11 percent of the original oil-in-place is expected to be recovered, extending the estimated life of the pool from six to 20 years.

Avon Hill Saskoil had a minor interest (2.5 percent) in the Avon Hill waterflood, located in west central Saskatchewan. Over the course of the year, 49 wells were drilled to implement this waterflood.

Waterflood Optimization

Throughout Saskatchewan, operators have started to optimize production from existing waterfloods, including many that were established in the mid to late 1950's. In order to increase the efficiency of waterflooding, optimization may include the drilling of additional wells and/or the modification of equipment and facilities.

The benefits of such activity include increased oil production, extended pool life, and reduced royalties on new reserves.

During 1985, Saskoil invested $1.8 million in waterflood optimization programs at nine Saskatchewan locations. In addition, we proposed a three phase optimization project as operator and major owner of the Bone Creek Unit in southwest Saskatchewan. Pending final partner and government regulatory approvals, the $2.9 million first phase will proceed in 1986.

During 1985, Saskoil completed the $14 million Marsden Waterflood Project. The project is expected to more than double recoverable reserves. ▼

DEVELOPMENT

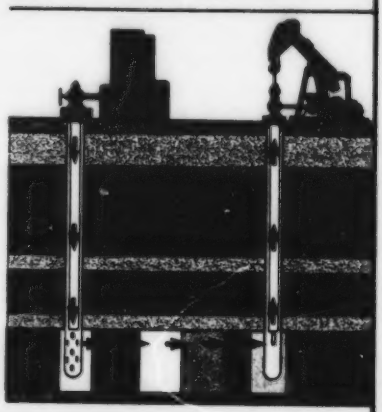
Enhanced Oil Recovery

This is a term applied to various "exotic" recovery techniques that inject substances such as air/oxygen, steam, or gas into a reservoir in order to stimulate incremental production. Although there is a tendency to consider enhanced oil recovery techniques as applicable only to heavy oil pools, the technology can also yield excellent results when applied to light and medium oil pools.

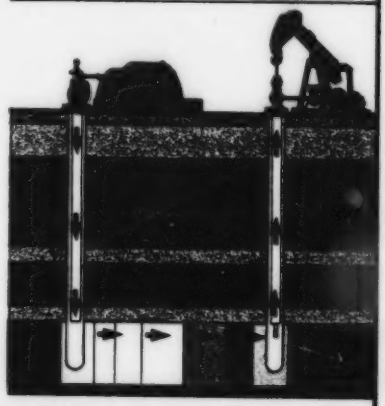
Battrum Located south of Swift Current, the three Battrum units employ an enhanced oil recovery technique that has been a commercial success in the Battrum field for over 20 years. Known as "fireflooding", this technique is applied by injecting air into the reservoir and then igniting a portion of the reservoir's oil. The resulting combustion heats the remaining oil and drives it to the producing wells in the field. Saskoil's average 21 percent working interest in the units provides approximately 19 percent of the company's proven reserves. This is the largest concentration of reserves that we have in any one pool..

RECOVERY METHODS

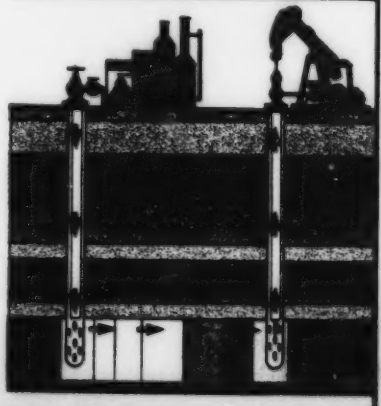
WATERFLOODING performed by injecting high pressure water into a reservoir, thereby flushing the oil to producing wells.



STEAMFLOODING performed by injecting steam into the reservoir which condenses upon contact with the cooler formation sands. The resulting hot water reduces the viscosity of the oil, allowing it to flow to the producing wells.



FIREFLOODING performed by injecting air into a reservoir and then igniting a portion of the reservoir's oil. The resulting combustion heats the remaining oil and drives it to the producing wells.



During 1985, major improvements were made to the Battrum facilities, with Saskoil's share of the cost at $2.4 million. In addition to increasing efficiency and extending the life of existing operations, the improvements make the expansion of flood patterns possible and allow us to maximize our recovery from the field. Drilling required to expand patterns is scheduled for 1986.

North Battleford Heavy Oil Project Saskoil has a one-third interest in this pilot steam project. In its tenth year, the project is currently too small to convert to a commercial operation. In an effort to determine reserves and the feasibility of expansion, eight wells were drilled within eight kilometres of the pilot site. Drilling failed to establish the reserves needed to support expansion and the program was terminated.

At present, we are evaluating our participation in this project and the value of the information it is providing us. During 1986, a decision will likely be made pertaining to our future level of involvement.

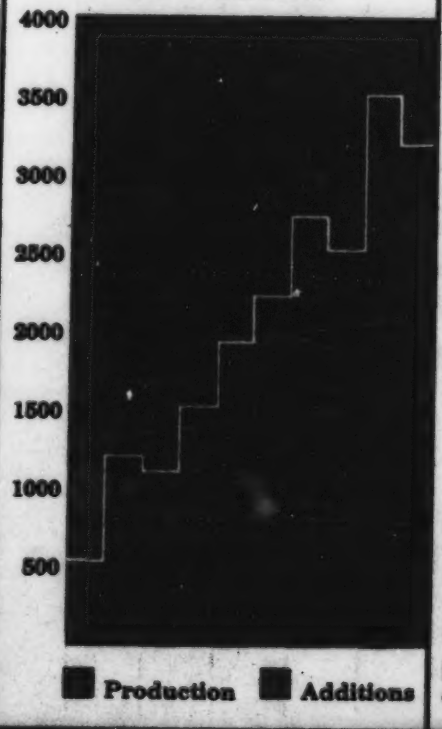
Onion Lake Saskoil holds a 100 percent interest in five thousand hectares at Onion Lake, located 45 kilometres north of Lloydminster. Discovered in 1978, the reservoir is saturated with oil that is too heavy to produce under primary recovery. Based on the characteristics of the reservoir and on a successful steam stimulation test in 1984, the pool is considered to have excellent potential for an enhanced oil recovery scheme.

Saskoil is presently talking with potential joint venture partners about development of the project. If partnership arrangements can be settled, Onion Lake could develop into a large, commercial enhanced oil recovery program.

Senlac Studies suggest that Senlac, Saskoil's largest operated heavy oil pool, is unlikely to respond successfully to waterflooding. In order to sustain and increase production from Senlac, it is necessary to evaluate the feasibility of recovery techniques in the pool while it is still producing under primary recovery. In response to this, a detailed design of an oxygen-injection pilot was completed by late 1985. Pending partner and regulatory approvals, this pilot will become operational in 1986.

PRODUCTION VS ADDITIONS

(Cumulative Oil Production VS Reserve Additions by Development — thousands of cubic metres)



OIL AND GAS FACILITY CONSTRUCTION

During 1985, $5.9 million were spent on the construction of oil and gas facilities. This included the completion or expansion of several major oil treating facilities in fields producing under primary recovery. At locations such as Court, Plover Lake, and Neilburg, we improved our ability to treat and move our heavy oil by completing expansion programs that began in 1984.

In addition to oil facilities, Saskoil proceeded with the construction of several fuel gas and gas sales systems. Fuel gas systems gather natural gas that is produced in association with the production of oil. This gas is then used to fuel pumpjack motors and heat oil storage tanks. By comparison, a gas sales system collects and processes gas for marketing.

Gas systems were installed at Senlac, Nottingham, Cantuar, and Beverley.

PRODUCTION

In 1985, we recorded our second best year of production. A total of 779 thousand cubic metres was produced — off slightly from last year's record of 819 thousand cubic metres.

During the first and fourth quarters of 1985, Saskatchewan oil producers were faced with reduced market demands and/or overburdened pipelines. As a result of these conditions, Saskoil (along with other producers) had to cut back production in some regions from five to 20 percent.

The periodic marketing and transportation problems that are confronting the industry force producers to find solutions. We are resolving these problems by reviewing transportation investment opportunities, becoming more active in pipeline affairs, and negotiating new contracts with joint venture operators who purchase as well as operate. By pursuing these contracts, we can diversify our markets and ensure that our production moves with that of our joint venture operators.

Saskoil's 1985 production was second only to the record set in 1984. ▼

DEVELOPMENT

Production Streams

During the year, light and medium oil production figures totalled 476 thousand cubic metres, with 273 thousand cubic metres produced from the Swift Current area and 180 thousand cubic metres produced from the Weyburn-Estevan area.

The Kindersley-Kerrobert region of west central Saskatchewan provided 213 thousand cubic metres of production with all but 4.5 percent being heavy oil. The remaining 10 thousand cubic metres was light oil produced from shallow Viking formations. The Lloydminster area of northwest Saskatchewan provided 96 thousand cubic metres of heavy oil production. Wells in Alberta and Manitoba also contributed to the year's production with figures reaching 17 thousand cubic metres — an increase of 35 percent from 1984.

In 1985, our natural gas production increased to 20 million cubic metres from 16 million cubic metres in 1984. With this rise in production, we realized net gas revenues in excess of $1 million for the first time in our history. Several more gas sales projects are planned for 1986.

RESERVES

During 1985, 99 percent of our proven producing reserves were located in our four producing districts in Saskatchewan. Proven producing reserve additions amounted to 621 thousand cubic metres of oil — an 80 percent replacement of the year's production. Saskoil uses only proven producing oil and gas reserves when determining annual depletion rates.

It is also company philosophy not to book reserve additions from infill wells drilled in 1985 until the production performance of wells verifies that incremental volumes are being recovered from the pools.

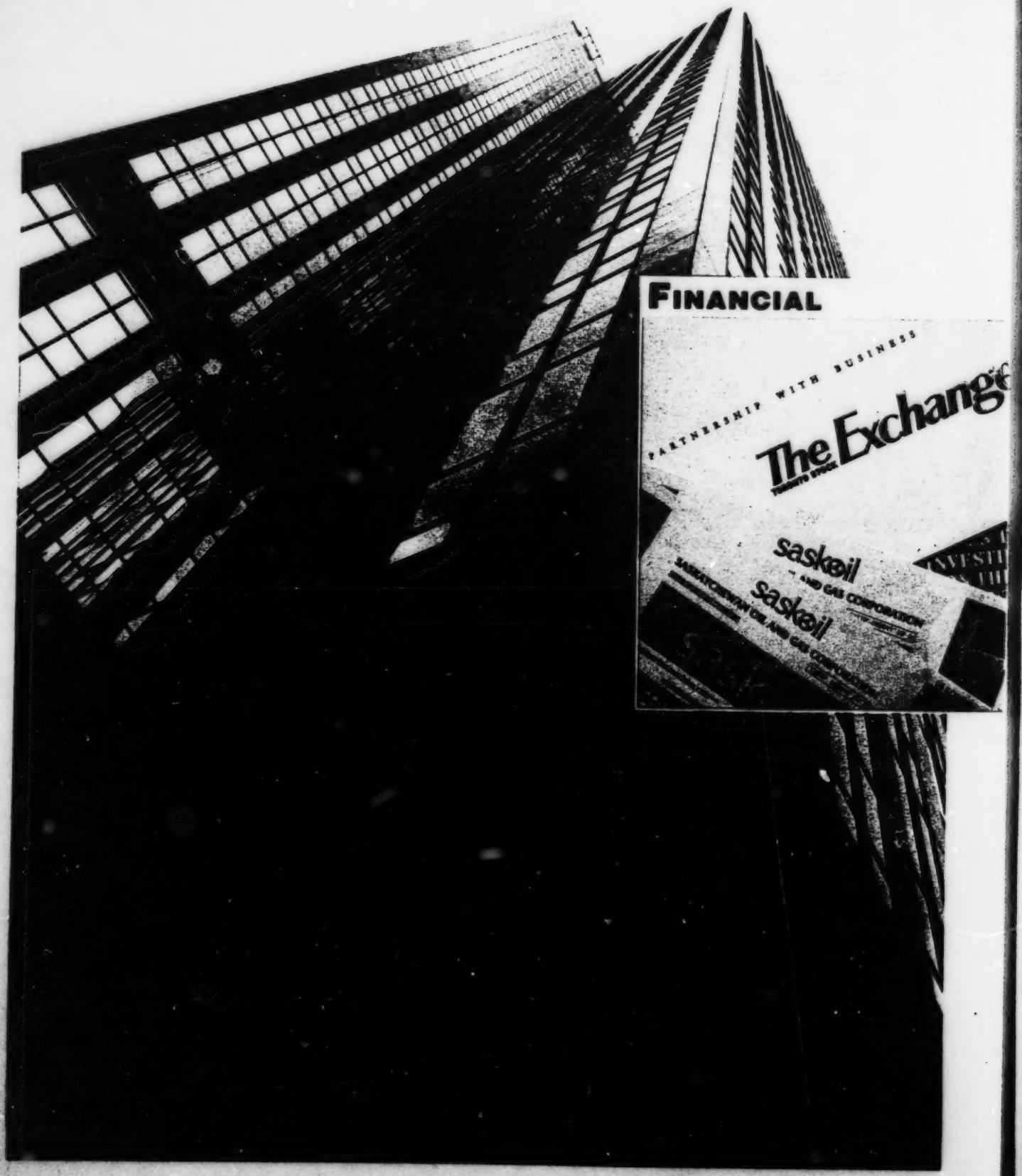
For the second year, we contracted for an independent appraisal of our reserves by the consulting firm of Coles Nikiforuk Pennell Associates Ltd. The appraisal was conducted in order to fulfill information requirements associated with the share offering. The report's findings resulted in a downward adjustment to heavy oil reserves that was partially offset by an increase in light and medium reserves.

At year end, our proven producing reserves stood at 6.87 million cubic metres, or nine times 1985's production levels. Over the past five years, we have produced 3.5 million cubic metres of oil while strengthening our reserve base with the addition of 3.3 million cubic metres. These reserves provide us with excellent production stability for the future.

TOTAL RESERVES

(December 31, 1985)

	Oil (thousands of cubic metres)				Gas (millions of cubic metres)	
	Gross Before Royalties			Net of Royalties	Gross Before Royalties	Net of Royalties
	Light & Medium	Heavy	Total	Total	Total	Total
Proven Producing						
At December 31, 1984	5,503	1,783)	7,286)		65	
Adjustments	189	(452)	(263)		6	
Additions	244	377	621		6	
	5,936	1,708	7,644		77	
Less: Production	476	303	779		20	
Reserves at December 31, 1985	5,460	1,405	6,865	4,819	57	48
Proven Non-Producing:	455	99	554	399	800	694
Probable:	2,432	1,380	3,812	2,745	352	310
Total Proven Plus Probable:	8,347	2,884	11,231	7,963	1,209	1,052


FINANCIAL
PARTNERSHIP WITH BUSINESS
The Exchange
saskoil
saskoil

FINANCIAL REVIEW

"Saskoil finished 1985 in a strong financial position with negligible debt and high liquidity. Completion of the share issue in 1986 brought further improvement. The company is well positioned financially to withstand short term price fluctuations and pursue attractive opportunities."

Harold Johnson
Vice-President, Finance and
Chief Financial Officer

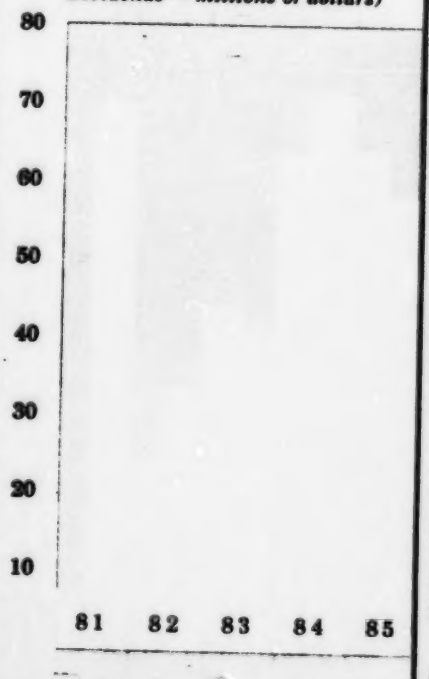
arnings for 1985 were $40.6 million, a decrease of $3.4 million from the record high in 1984 of $44 million.

Net sales revenue was up $2.5 million with five percent lower production being more than offset by higher average prices and lower royalty costs. Interest income rose $1.7 million due to higher cash balances.

Total expenses rose $7.6 million to $78.6 million. Operating and administration costs were $4.2 million higher as more wells were added to the production system and a one-time charge of $1.5 million was made for a research facility transferred to a crown agency for a nominal amount. Rising costs of finding and developing oil reserves increased the cost per cubic metre and resulted in $2.6 million higher costs for depletion, depreciation and amortization. Petroleum and Gas Revenue Tax declined $1 million as a result of the provisions of the Western Accord. A full year's interest on the Participation Bonds issued in November, 1984 raised interest costs by $1.8 million.

FUNDS VS EXPENDITURES

(Funds From Operations VS Capital Expenditures and Dividends — millions of dollars)

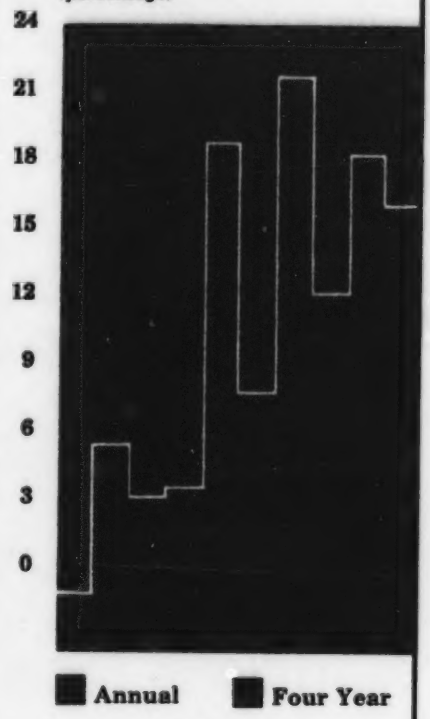


Saskoil became subject to income tax on December 14, 1985 and recorded tax, all deferred, of $1.4 million to the end of the year. The company has deductions available for income tax purposes which are in excess of the related book value as stated in note four to the Consolidated Financial Statements. The use of this excess cost to reduce income tax is reflected as an extraordinary item of $1.4 million in 1985 and this treatment will continue in future years.

Capital expenditures rose $14.6 million to $58.8 million reflecting a more aggressive exploration and development program and investments to improve production from existing reserves. Funds from operations of $64 million fully financed the capital program.

RETURN ON AVERAGE CAPITAL EMPLOYED

(percentage)



The annual return on average capital employed was 18.3 percent, resulting in a four year average of 16.3 percent, which exceeded the corporate objective of 14 percent.

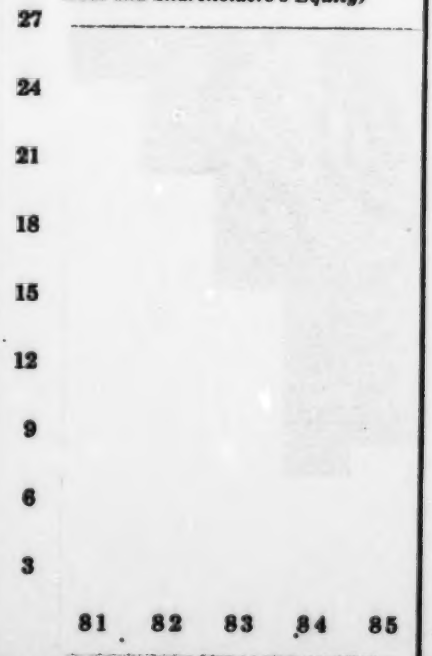
Saskoil was in a strong financial position at year end with $22.4 million of working capital and $15 million of debt, made up of Participation Bonds due in 1990. A $25 million loan from the Province of Saskatchewan became due and was paid in November, 1985.

In December, Saskoil issued common shares to Crown Investments Corporation of Saskatchewan in exchange for its outstanding equity advances in preparation for the public share offering completed in January, 1986. The public issue raised $110 million which provided $28.7 million to Saskoil after payment of issue costs and a $75 million dividend to Crown Investments Corporation of Saskatchewan. This financing has further strengthened the company's financial position. Long term debt as a percentage of debt and shareholders' equity was 5.3 percent after completion of the public share issue.

Saskoil's financial position will enable the company to capitalize on attractive investment opportunities despite a difficult economic environment caused by oil price declines.

LONG TERM DEBT

(as a percentage of Debt and Shareholders's Equity)



MANAGEMENT REPORT

The accompanying consolidated financial statements and all information in the Annual Report are the responsibility of management. The consolidated financial statements of Saskatchewan Oil and Gas Corporation have been prepared by management in accordance with accounting principles generally accepted in Canada, including amounts that are based on informed judgements and management estimates. Other financial information in the Annual Report is consistent with that in the consolidated financial statements.

Management maintains an appropriate system of internal controls to provide reasonable assurance that transactions are authorized, assets are safeguarded and financial records are properly maintained to provide reliable information in the preparation of financial statements and other data.

The Corporation's external auditors, Clarkson Gordon, have examined the consolidated financial statements, and their report thereon is set out below.

The Audit Committee of the Board, which is comprised of directors who are not employees of the Corporation, has reviewed the consolidated financial statements, including the notes thereto, with management and both the internal and the external auditors. The consolidated financial statements have been approved by the Board of Directors on the recommendation of the Audit Committee.

AUDITORS' REPORT

To the Shareholders of Saskatchewan Oil and Gas Corporation

We have examined the consolidated statement of financial position of Saskatchewan Oil and Gas Corporation as at December 31, 1985 and the consolidated statements of earnings, retained earnings, and changes in financial position for the year then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests and other procedures as we considered necessary in the circumstances.

In our opinion, these consolidated financial statements present fairly the financial position of the Corporation as at December 31, 1985 and the results of its operations and the changes in its financial position for the year then ended in accordance with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

Regina, Canada
March 3, 1986

Chartered Accountants

CONSOLIDATED STATEMENT OF FINANCIAL POSITION AS AT DECEMBER 31, 1985

	1985	1984
	(thousands of dollars)	
Assets		
Current Assets		
Cash, including short-term investments	$ 24,202	$ 45,193
Accounts receivable	26,104	25,927
Inventories and prepaid expenses	3,929	3,732
	54,235	74,852
Property and Equipment (note 5)	229,850	198,462
Unamortized Bond Issue Costs	444	575
	$284,529	$273,889
Liabilities		
Current Liabilities		
Accounts payable and accrued liabilities	$ 22,062	$25,199
Petroleum and gas revenue tax	9,765	3,214
Dividend payable	—	6,605
8.5% Province of Saskatchewan loan	—	25,000
	31,827	60,018
Deferred Gas Revenue	322	337
Dividend Payable (notes 2 & 6)	75,000	—
Participation Bonds (note 7)	15,000	15,000
	122,149	75,355
Shareholder's Equity		
Share Capital (formerly Equity Advances — notes 2 & 3)	145,500	145,500
Retained Earnings	16,880	53,034
	162,380	198,534
	$284,529	$273,889

Approved by the Board:

Director **Director**

CONSOLIDATED STATEMENTS OF EARNINGS AND RETAINED EARNINGS

CONSOLIDATED STATEMENT OF EARNINGS FOR THE YEAR ENDED DECEMBER 31, 1985

	1985	1984
	(thousands of dollars)	
Revenue		
Crude oil and natural gas sales	$161,120	$160,935
Less royalties	47,888	50,251
Net sales revenue	113,232	110,684
Interest and other income	5,975	4,309
	119,207	114,993
Expenses		
Operating and administration	38,889	34,681
Depletion, depreciation and amortization	21,801	19,162
Petroleum and gas revenue tax	13,508	14,544
Interest (note 8)	4,386	2,573
	78,584	70,960
Earnings Before Income Taxes and Extraordinary Item	40,623	44,033
Income Taxes — Deferred (notes 2 & 4)	(1,400)	—
Earnings Before Extraordinary Item	39,223	44,033
Extraordinary Item (note 4)	1,400	—
Earnings	**$ 40,623**	$ 44,033

CONSOLIDATED STATEMENT OF RETAINED EARNINGS FOR THE YEAR ENDED DECEMBER 31, 1985

	1985	1984
	(thousands of dollars)	
Retained Earnings, Beginning of Year	$ 53,034	$ 15,606
Earnings	40,623	44,033
Public Share Issue Costs (note 2)	(1,777)	—
Dividends (notes 2 & 6)	(75,000)	(6,605)
Retained Earnings, End of Year	**$ 16,880**	$ 53,034

CONSOLIDATED STATEMENT OF CHANGES IN FINANCIAL POSITION FOR THE YEAR ENDED DECEMBER 31, 1985

	1985	1984
	(thousands of dollars)	
Funds Provided From:		
Operations		
Earnings before Extraordinary Item	$ 39,223	$ 44,033
Items not requiring outlay of funds (note 9)	24,771	19,545
Funds from Operations	63,994	63,578
Government incentives (note 5)	3,521	3,425
Proceeds from disposal of Property and Equipment	649	773
	68,164	67,776
Funds Used For:		
Additions to Property and Equipment	58,813	44,217
Dividends (notes 2 & 6)	—	26,605
	58,813	70,822
Funds Provided (Used) Before Financing Activities	9,351	(3,046)
Funds Provided From (Used For) Financing Activities:		
Conversion of equity advances to share capital (note 2)	145,500	—
Equity advances	(145,500)	20,000
Public share issue costs (note 2)	(1,777)	—
Province of Saskatchewan loan	—	(25,000)
Bond issue	—	15,000
Bond issue costs	—	(561)
	(1,777)	9,439
Increase in Working Capital	**7,574**	6,393
Working Capital, Beginning of Year	14,834	8,441
Working Capital, End of Year	**$ 22,408**	$ 14,834

1. Summary of Significant Accounting Policies

The consolidated financial statements of Saskatchewan Oil and Gas Corporation ("Saskoil" or the "Corporation") have been prepared in accordance with generally accepted accounting principles. A precise determination of certain assets and liabilities is dependent upon future events; therefore, the preparation of financial statements involves the use of estimates. The more significant accounting policies are summarized below.

Principles of Consolidation

The consolidated financial statements include the accounts of Saskatchewan Oil and Gas Corporation and its wholly-owned subsidiaries, Saskoil Resources Inc. and Consumers Oil Limited.

Substantially all exploration and production activities are conducted jointly with others. The consolidated financial statements reflect only Saskoil's proportionate interest in such activities.

Full Cost Method of Accounting

Saskoil follows the full cost method of accounting whereby all costs related to exploration and development of oil and gas reserves, whether productive or non-productive, are capitalized. Such costs include lease acquisition costs, geological and geophysical expenditures, rentals on undeveloped properties, costs of drilling both productive and non-productive wells and overhead expenditures related to exploration activities. Costs net of accumulated depletion and depreciation are limited to undiscounted future net revenues from proven producing reserves based on current prices and costs, plus the lower of cost and fair market value of non-producing properties.

Proceeds from property and equipment dispositions are applied against the net book value of property and equipment without recognizing any gain or loss on disposition unless such a disposition would significantly alter the relationship between capitalized costs and proven producing reserves. Gains and losses on other property and equipment dispositions are recognized in the statement of earnings.

Enhanced Oil Recovery

Costs of enhanced oil recovery processes prior to the establishment of commercially viable projects are expensed as incurred. Costs of viable projects are charged to the full cost pool.

Depletion, Depreciation and Amortization

Depletion of costs capitalized under the full cost method of accounting and depreciation of wellhead equipment, field equipment and buildings, tanks and flowlines are calculated using the unit-of-production method based on estimated recoverable proven producing reserves of oil and gas as determined by corporate or independent engineers.

Depreciation of other equipment is calculated at rates which will charge original costs to operations over the estimated useful lives of the respective assets using the straight-line method.

Leasehold improvements are amortized over the remaining terms of leases in effect.

Bond issue costs are amortized to interest expense over the life of the bonds.

Inventories

Inventories are valued at the lower of weighted average cost and replacement value.

Government Incentives

Government incentives are deducted from the expenditures to which they relate.

2. Public Participation

The events described below occurred during December 1985 and January 1986, the result of which has been a change in status of Saskoil from a crown corporation to a crown-controlled corporation with significant public ownership.

(a) On December 3, 1985 a $91.5 million equity advance was received from Crown Investments Corporation of Saskatchewan and used to repay a $91.5 million equity advance previously received from the Saskatchewan Heritage Fund.

(b) On December 13, 1985 Saskoil was continued under the provisions of The Business Corporations Act (Saskatchewan) and became a corporation with share capital.

(c) On December 14, 1985 Saskoil ceased to be exempt from federal and provincial income taxes as a result of granting to each of its five senior officers an option for the purchase of one common share.

(d) On December 16, 1985 the Province of Saskatchewan's $145.5 million equity advances through Crown Investments Corporation of Saskatchewan were converted into 15,842,910 common shares.

(e) On December 16, 1985 a $75.0 million dividend was declared to Crown Investments Corporation of Saskatchewan payable from the net proceeds of the public share offering described below.

(f) On January 14, 1986 Saskoil completed an issue to the public of 3,793,104 units, each consisting of one common share and two second preferred shares, at a price of $29.00 per unit. Net proceeds were $103.7 million after deducting an underwriting commission of $4.5 million and other share issue costs of $1.8 million incurred in 1985.

2. Public Participation *(continued)*

Below is a condensed consolidated statement of financial position comparing reported year end and pro forma amounts adjusted for the public share issue proceeds net of the underwriting commission as described in (f) and payment of the dividend described in (e).

Pro Forma Condensed Consolidated Statement of Financial Position As At December 31, 1985

	Actual	Effects of Above Transactions	Pro Forma
Assets			
Current	$ 54,235	$ 30,500	$ 84,735
Other	230,294	—	230,294
Total	$284,529	$ 30,500	$315,029
Liabilities			
Current	$ 31,827	$ —	$ 31,827
Other	90,322	(75,000)	15,322
	122,149	(75,000)	47,149
Shareholders' Equity			
Share Capital	145,500	110,000	255,500
Retained Earnings	16,880	(4,500)	12,380
	162,380	105,500	267,880
Total	$284,529	$ 30,500	$315,029

3. Share Capital

The share capital at December 31, 1985 and at January 14, 1986, the date of completion of the public share issue, is as follows:

	December 31, 1985		January 14, 1986	
	Shares Issued	Amount	Shares Issued	Amount
First preferred	none	$ —	none	$ —
Second preferred	none	—	7,586,208	75,862
Common	15,842,910	145,500	19,636,014	179,638
Total		$145,500		$255,500

The second preferred shares have voting privileges and are entitled to cumulative dividends of $0.725 per share per annum. These shares are convertible into common shares at the option of the holder at a rate of conversion of 1.0 common share for each preferred share prior to the close of business on December 31, 1988 and at a rate of 0.833 thereafter until the close of business on December 31, 1995.

The second preferred shares are redeemable at the option of Saskoil after the close of business on December 31, 1988 and prior to the close of business on December 31, 1990, depending on future prices of the common shares on The Toronto Stock Exchange. Thereafter, the shares are redeemable at prices declining $0.20 per share annually from $11.00 to $10.00.

The Saskatchewan Oil and Gas Corporation Act, 1985 prohibits any person or group of associated persons, other than the Province of Saskatchewan, from owning more than 4% of the issued and outstanding voting shares of Saskoil. In addition, the Act provides that holders of voting shares of Saskoil must be Canadian citizens or residents.

Saskoil was a wholly owned subsidiary of a crown corporation at December 31, 1985, accordingly earnings per share are not provided.

4. Income Taxes and Extraordinary Item

Saskoil is entitled to deduct from taxable income certain expenditures previously incurred, portions of which have been charged to earnings in prior years. As a result, there are expenditures to be claimed for tax purposes in excess of those remaining in the accounts. The estimated amount of the excess expenditures at December 31, 1985 is $96 million.

The extraordinary item of $1.4 million reduces income taxes to nil as a result of claiming a part of these excess expenditures. The utilization of the excess in future periods will continue to be recognized as an extraordinary item.

5. Property and Equipment

	1985			1984
	Cost	Accumulated Depletion, Depreciation, Amortization	Net Book Value	Net Book Value
Petroleum and natural gas leases and rights together with exploration and development thereon	$240,530	$ 85,638	$154,892	$136,991
Production equipment	97,216	27,083	70,133	54,471
Other equipment	9,969	5,144	4,825	7,000
	$347,715	**$117,865**	**$229,850**	$198,462

During the year, Saskoil earned $3.5 million of incentive grants under the Saskatchewan Oil and Gas Regulations, 1978. This program has been discontinued.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 1985 (tabular figures in thousands of dollars)

6. Dividends

In 1985 Saskoil declared a dividend of $75.0 million payable to Crown Investments Corporation of Saskatchewan ("CIC"), to be paid from the proceeds of the public share issue in January, 1986.

In 1984 a dividend of $6,605,000 was declared and paid to CIC.

In 1983 a dividend of $30.0 million was declared payable to CIC. Of this amount, $20.0 million was paid in 1984 concurrent with receipt of a $20.0 million equity advance from CIC.

7. Participation Bonds

The bonds mature March 31, 1990, and are guaranteed as to principal and interest by the Province of Saskatchewan. Interest is payable March 31 of each year at 10% plus .03 percentage points for each $1 million of corporate Net Sales Revenue.

The interest rate for the period November 14, 1984 to March 31, 1985 is 13.3% and for the year ending March 31, 1986 is 13.4%.

The bonds carry a right of redemption at the option of Saskoil at prices of $1,080 and $1,050 per $1,000 of bond principal on March 31, 1988 and 1989, respectively.

8. Interest Expense

	1985	1984
Interest on Participation Bonds and Province of Saskatchewan loan	$ 3,909	$ 2,420
Other interest	477	153
	$ 4,386	$ 2,573

9. Items not requiring outlay of funds

Non-fund items:

	1985	1984
Depletion, depreciation and amortization	$21,801	$19,162
Research facility charged to expense	1,454	—
Amortization of bond issue costs	131	46
Income taxes — deferred	1,400	—
Deferred gas revenue	(15)	337
	$24,771	$19,545

10. Commitments

Minimum lease payments under operating leases for office space and equipment in thousands of dollars:

1986	$ 2,600
1987	2,600
1988	2,500
1989	2,300
1990	1,800
	$11,800

11. Employee Pension Plan

Under Saskoil's pension plan arrangements, employee contributions are matched by the Corporation and these amounts are contributed to money-purchase pension plans. As a result, there are no unfunded pension plan liabilities and no outstanding corporate obligations.

12. Related Party Transactions

The consolidated financial statements include capital, revenue and expense amounts resulting from routine operating transactions conducted at prevailing market prices with various Saskatchewan crown controlled departments, agencies and corporations with which Saskoil is related. Account balances resulting from these transactions are included in the consolidated statement of financial position and are settled on normal trade terms.

Certain information as to related party transactions is not available by virtue of the fact that Saskoil conducts a substantial portion of its exploration and production activities through joint ventures which are not contractually required to report Saskoil's share of routine operating transactions with Saskoil related parties.

In August 1985 Saskoil transferred a research facility to an agency of the Province of Saskatchewan for a nominal amount. The net book value of $1.5 million was charged to operating and administration expenses.

In December 1985 Saskoil transferred certain properties with an estimated value of $6.7 million to a Saskatchewan crown corporation in exchange for properties of equivalent value.

In December 1985 Saskoil sold a $5.4 million short-term investment to a Saskatchewan crown-controlled corporation for equivalent cash consideration.

SASKOIL

FIVE YEAR SUMMARY

FINANCIAL

	1985	1984	1983	1982	1981
					(thousands of dollars)
Revenue					
Crude oil and natural gas sales	$161,120	$160,935	$136,047	$103,968	$ 60,014
Less royalties	(47,888)	(50,251)	(48,142)	(37,180)	(26,210)
Interest and other income	5,975	4,309	3,247	1,813	729
	119,207	114,993	91,152	68,601	34,533
Less Expenses					
Operating and administration	38,889	34,681	33,725	31,022	20,461
Depletion, depreciation and amortization	21,801	19,162	12,974	11,639	13,111
Petroleum and gas revenue tax	13,508	14,544	10,222	8,536	3,686
Interest	4,386	2,573	3,302	4,548	3,481
Income taxes — deferred	1,400	—	—	—	—
Earnings (Loss) Before the Following	39,223	44,033	30,929	12,856	(6,206)
Unusual items	—	—	—	(11,288)	—
Extraordinary item	1,400	—	—	—	—
Earnings (Loss)	$ 40,623	$ 44,033	$ 30,929	$ 1,568	$ (6,206)
Funds Provided From:					
Operations	$ 63,994	$ 63,578	$ 43,936	$ 24,528	$ 6,938
Government incentives	3,521	3,425	3,580	3,629	2,671
Proceeds from disposal of property and equipment	649	773	1,155	462	276
Equity financing	—	20,000	—	31,000	40,500
Long term debt financing	—	15,000	—	—	—
	68,164	102,776	48,671	59,619	50,385
Funds Used For:					
Additions to property and equipment	58,813	44,217	30,080	31,031	69,792
Dividends	—	26,605	10,000	1,568	—
Long term debt retirement	—	25,000	10,000	—	—
Financing costs	1,777	561	—	—	—
	60,590	96,383	50,080	32,599	69,792
Increase (Decrease) in Working Capital	$ 7,574	$ 6,393	$ (1,409)	$ 27,020	$(19,407)
Financial Position					
Working capital	$ 22,408	$ 14,834	$ 8,441	$ 9,850	$(17,170)
Property and equipment	229,850	198,462	177,605	165,234	161,221
Long term debt	15,000	15,000	25,000	35,000	35,000
Shareholder's equity	162,380	198,534	141,106	140,177	109,177
Financial Ratios					
Royalties as % of sales	29.7%	31.2%	35.4%	35.8%	43.7%
Working capital ratio	1.7:1	1.2:1	1.3:1	1.4:1	0.6:1
Return on average capital employed	18.3%	21.8%	18.9%	3.1%	—
Four year return on average capital employed	16.3%	12.2%	7.8%	3.5%	5.5%

PRODUCTION AND RESERVES	1985	1984	1983	1982	1981
					(gross before royalties)
Production					
Oil (thousands of m³)					
Light/Medium oil	476	481	455	387	355
Heavy oil	303	338	293	247	182
Total oil	779	819	748	634	537
Gas (millions of m³)	20	16	10	4	11
Proven Producing Reserves*					
Oil (thousands of m³)					
Light/Medium oil	5,460	5,503	7,320	6,335	4,407
Heavy oil	1,405	1,783	1,847	1,335	1,301
Total oil	6,865	7,286	9,167	7,670	5,708
Gas (millions of m³)	57	65	744	1,149	1,219
Changes in oil reserves (thousands of m³):					
Reserves, beginning of year	7,286	9,167	7,670	5,708	5,014
Additions by development	621	349	676	331	1,231
Revisions of previous estimates	(263)	(1,411)	1,569	2,265	—
Production	(779)	(819)	(748)	(634)	(537)
Reserves, end of year	6,865	7,286	9,167	7,670	5,708
Proven Non-Producing Reserves					
Oil (thousands of m³)	554	691	—	—	—
Gas (millions of m³)	800	433	—	—	—
Probable Reserves					
Oil (thousands of m³)	3,812	3,241	—	—	—
Gas (millions of m³)	352	477	—	—	—
Statistics					
Drilling (gross wells)	652	429	253	160	268
Average oil price ($/m³)	205.13	196.00	182.77	163.19	108.71
Number of employees, end of year	284	259	247	315	285

* Prior to 1984, the Corporation reported and based its depletion calculation on proven developed reserves. For 1984, the Corporation adopted the reporting of proven producing reserves. While it is not practical to recalculate reserves for all previous years, the Corporation has determined that the difference between proven producing and proven developed reserves at the end of 1984 and 1983 is not material.

SHAREHOLDERS' INFORMATION

Canadian Shareholders

The common and convertible preferred shares are traded on the Toronto Stock Exchange and the Montreal Exchange. As of March 3, 1986, there were 6,534 registered holders of common shares, and 6,416 registered holders of convertible preferred shares.

Dividends

On March 3, 1986, the Board of Directors declared the first quarterly dividend on the convertible preferred shares of $0.1531 per share, which was pro-rated and payable March 31, 1986 to shareholders of record on March 14, 1986.

Common Shares

Transfer Agent and Registrar

The Royal Trust Company

Regina, Montreal, Toronto, Winnipeg, Calgary, and Vancouver

Listed

Toronto Stock Exchange
Toronto, Canada

Montreal Exchange
Montreal, Canada

Symbol: "SKO"

Convertible Preferred Shares

Transfer Agent and Registrar

The Royal Trust Company

Regina, Montreal, Toronto, Winnipeg, Calgary, and Vancouver

Listed

Toronto Stock Exchange
Toronto, Canada

Montreal Exchange
Montreal, Canada

Symbol: "SKO PR A"

Dividends

The holders of convertible preferred shares will be entitled to fixed cumulative preferential cash dividends as and when declared by the Board of Directors at a rate of $0.725 per share per annum payable quarterly on March 31, June 30, September 30, and December 31.

Conversion Privilege

Each convertible preferred share is convertible into common shares of Saskoil at the option of the holder prior to the close of business on December 31, 1988 at a conversion price of $10.00 per common share and, after December 31, 1988 and prior to the close of business on December 31, 1995, at a conversion price of $12.00 per common share, subject to adjustment in certain events.

Auditors

Clarkson Gordon
Chartered Accountants
Regina, Canada

Shareholder Services

Mark A. Pinvidic
1000, Saskoil Tower
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P.O. Box 1550
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S4P 3C4

(306) 787-9700

Annual Meeting

The annual general meeting of the shareholders will be held at the Hotel Saskatchewan, Regina, Saskatchewan, Canada on Monday, May 5, 1986 at 2:00 p.m.

Stock Exchange Information

A variety of informational publications are available from the Toronto Stock Exchange at no charge. The list includes the following:

- How to Read Newspaper Listings
- Glossary of Investment Terms
- Fact Sheet
- The TSE Composite Index
- Trader's Market
- You Can Participate in Business Expansion
- Daily Record
- Tune In to the Toronto Stock Exchange
- The Visitors Centre

In addition to these publications, the Toronto Stock Exchange offers a public tour of the exchange including a multi-image slide show, market discussion and demonstration of the TSE's computerized information system. The presentation is 45 minutes in length and is held Monday to Friday at 2:00 p.m.

To order any of the above publications or if you require further information on the TSE's presentations, call or write:

Sharon Ofiara
Public Affairs Department
The Exchange Tower
Two First Canadian Place
Toronto, Ontario, Canada
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(416) 947-4670

CORPORATE INFORMATION

Saskatchewan Oil and Gas Corporation (a Canadian corporation)

Trademark

Saskatchewan Oil and Gas Corporation holds the saskoil trademark

Directors

Herbert C. Pinder, Jr., (1)
Chairman
President, Herbus Holdings Ltd.
Saskatoon, Saskatchewan

Theodore M. Hanlon, (1)
Vice-Chairman
President, Crescendo Oil and Gas
Calgary, Alberta

Robert G. Bentall
President, The Bentall Group
West Vancouver, British Columbia

William J. Brennan (2)
Dean of Commerce, University of Saskatchewan
Saskatoon, Saskatchewan

William J. Douglas (1)
President and Chief Executive Officer, Saskatchewan Oil and Gas Corporation
Regina, Saskatchewan

Donald K. MacPherson, Q.C.
Senior Partner, MacPherson Leslie & Tyerman law firm
Regina, Saskatchewan

Theodore H. Renner
President, Precambrian Shield Resources Limited
Calgary, Alberta

Rose M. Richardson (2)
President, Fuhrman's Meats Ltd.
Regina, Saskatchewan

Garnet K. Wells (2)
President, Crown Management Board
Regina, Saskatchewan

Carl A. Wagner,
Secretary

(1) Member of the Executive Committee
(2) Member of the Audit Committee

Officers

William J. Douglas
President and Chief Executive Officer

Dale M. Christensen
Vice-President, Resource Development

J. Gerald Gribben
Vice-President, Human Resources and Corporate Services

Harold W. Johnson
Vice-President, Finance and Chief Financial Officer

Donald L. Tough
Vice-President, Exploration

Management

G. Bill Armstrong
General Manager, Development

Thomas S. Bamford
Manager, Special Projects

Kenneth D. Foat
Manager, Economics and Planning

Gary J. Follensbee
General Manager, Resource Recovery

Thomas F. Hunter
Manager, Audit

John Kuch
Manager, Systems and Computer Services

Arthur G. Lange
Manager, Geophysics

J. Douglas Macdonald
General Manager, Production

Ronald Misko
Manager, Exploration Geology

Randolf A. Thomsen
Manager, Land

Ronald J. Wagstaff
Comptroller

Dennis W. Ward
Manager, Financial Planning

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Annual Report

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